the conferees believed that the formerly tax-exempt organizations should not be taxed on unrealized appreciation or depreciation that accrued during the period the organization was not generally subject to income taxation. *Id*.

The Service has learned that some BCBS organizations are claiming annual or periodic loss deductions under § 165 of the Code with respect to certain intangible assets, including customer lists, provider networks, and workforce in place using the fair market value basis provided under § 1012(c)(3)(A)(ii) of the Act for purposes of determining gain or loss. For example, some BCBS organizations are claiming loss deductions in the year in which a customer terminates its relationship with the BCBS plan, on the theory that each customer relationship is a separate asset for federal income tax purposes.

The Service believes that BCBS organizations are not entitled to these loss deductions. In addition to carefully scrutinizing the valuations obtained for the assets at issue, the Service will challenge the loss deductions under various theories, as appropriate, including the following:

- These individual customer, provider, or employee contracts or relationships are not separate assets. The Supreme Court's decision in *Newark Morning Ledger Co. v. United States*, 507 U.S. 546 (1993), did not disturb earlier authority denying current loss deductions upon the termination of an individual customer, provider, or employee contract or relationship or similar component of a single asset. *See, e.g., Golden State Towel and Linen Service v. United States*, 373 F.2d 938 (Ct. Cl. 1967). In *Newark Morning Ledger*, the Supreme Court cited *Golden State Towel* with approval.
- Under the facts set forth above, annual or periodic loss deductions are the functional equivalent of amortizing the single assets composed of individual customer, provider, or employee contracts or relationships, and as such are contrary to Congress's express prohibition against using the § 1012(c)(3)(A)(ii) basis for amortization purposes. That is, some BCBS organizations are using these annual loss deductions as a mechanism for regularly converting a portion of a single intangible asset's § 1012(c)(3)(A)(ii) basis into an offset against current income, producing the same tax effect as amortizing that asset's § 1012(c)(3)(A)(ii) basis.
- By enacting § 1012 of the Act, Congress intended to take away the advantage the BCBS organizations enjoyed as tax-exempt entities in competing with commercial insurance companies by subjecting the BCBS organizations to the payment of federal income taxes to the same extent as commercial insurance providers. H.R. Rep. No. 426, 99th Cong., 1st Sess. 664 (1985). The legislative history to the Act indicates that Congress expected to remedy this inequity immediately, with the BCBS organizations beginning to pay tax in their initial years as taxable entities. The annual use of a portion of the § 1012(c)(3)(A)(ii) basis to offset a substantial amount of taxable income immediately upon becoming taxable would permit BCBS organizations to maintain the competitive advantage they enjoyed prior to the Act by effectively delaying for many years their obligation to pay federal income taxes to the same extent as other commercial insurance providers.
- By not having claimed loss deductions upon the termination of individual customer, provider, or employee contracts or relationships in prior years, BCBS organizations effectively adopted a method of accounting that treats customer lists, provider networks, and workforce in place as single assets composed of individual customer, provider, or employee contracts or relationships. A method of accounting cannot be changed without permission from the Secretary. Section 446(e); Rev. Rul. 90–38, 1990–1 C.B. 57. BCBS insurance organizations that file claims for refund to begin recovering the basis in individual customer, provider, or employee contracts or relationships that terminated in prior years are attempting to make an unauthorized change in method of accounting. *See* Treas. Reg. § 1.446–1(e)(2)(ii)(a).

DRAFTING INFORMATION

The principal author of this notice is Grace Matuszeski of the Office of the Associate Chief Counsel (Income Tax & Accounting). For further information regarding this notice contact Kay Hossofsky of the Office of the Associate Chief Counsel (Financial Institutions & Products) at (202) 622-3970 (not a toll-free call).

IRS Releases New Form 8871, *Political Organization Notice of Section 527 Status*

Notice 2000–36

The Internal Revenue Service on July 12, 2000, announced the release of the new form that section 527 political organizations must file and detailed plans for implementing other aspects of the new law governing these groups.

Starting immediately, section 527 political organizations must file Form 8871 with the IRS. This notice of organization must be filed by July 31, 2000.

The IRS action follows a new law approved last month by Congress and signed July 1, 2000, by President Clinton. The legislation creates a new set of rules for political organizations established under section 527 of the Internal Revenue Code. Under the new law, these 527 groups will be required to publicly disclose details about their organization, contributors, expenditures, annual returns and other information.

"The IRS is moving quickly to put these new rules in place. We want to make information from these organizations available to the public as soon as possible," IRS Commissioner Charles O. Rossotti said.

The IRS has also released new forms and other details involving reporting and disclosure requirements for 527 organizations.

The first step is the release of Form 8871, *Political Organization Notice of Section 527 Status*. The form is now available at the IRS web site, www.irs.gov, in the "Forms and Pubs" section.

Organizations must file Form 8871 both electronically and in writing. The form can be filed electronically at www.irs.gov/bus_info/eo/pol-file.html.

Every political organization under section 527 must file Form 8871 unless it reasonably expects annual gross receipts to always be less than $25,000 in each taxable year. Political committees also do not have to submit this form if they are required to file reports with the Federal Election Commission. Section 501(c) organizations such as social welfare groups, labor unions and trade associations that file Form 1120-POL and pay taxes under section 527(f)(1) also will not have to submit Form 8871.

The law requires newly established organizations to file Form 8871 within 24 hours of their creation. However, the IRS realizes some of these section 527 organizations may not yet be aware of this requirement. Consequently, the IRS has extended the due date for filing Form 8871 until July 31, 2000, for any organizations established after June 30, 2000. Organizations already in existence on June 30, 2000, already have until July 31, 2000, to file Form 8871.

Form 8871 contains a variety of information about 527 organizations, including the organization's purpose, a list of related entities, contact persons, record custodians, e-mail addresses and lists of officers, directors and highly compensated employees.

By August 15, 2000, the IRS will make available on its Internet site a list of organizations filing Form 8871. Copies of the Form 8871 will be available through the 527 organizations. The IRS is working on procedures to make copies of the forms available for public inspection as soon as possible.

The IRS has also released another form that 527 organizations will use to periodically disclose contributions and expenditures made after July 1, 2000. Form 8872, *Political Organization Report of Contributions and Expenditures*, will include names, addresses, employers and occupations for contributors of $200 or more annually. Organizations or individuals receiving $500 or more annually from 527 organizations also will be listed on these forms.

For more information about Form 8872, see Notice 2000–41, page 177.

Information from filed Forms 8872 will be available for public inspection.

The IRS also is in the process of determining which forms will be used as annual returns by 527 organizations with gross receipts of $25,000 or more. These returns also will be available for public review.

"Putting these new rules in place poses a major challenge for the IRS given the short time frame available," Rossotti said. "However, we are committed to serving taxpayers by implementing this important new law in a timely and convenient manner."

DRAFTING INFORMATION

The principal author of this notice is Judith E. Kindell of the Exempt Organizations Division. For further information regarding this announcement contact Judith E. Kindell on (202) 622-6494 (not a toll-free call).

Eligible Deferred Compensation Plans under Section 457

Notice 2000–38

I. PURPOSE AND SCOPE

This notice describes the withholding and reporting requirements "applicable to eligible deferred compensation plans described in § 457(b) of the Internal Revenue Code of 1986 ("§ 457(b) plans").

Specifically, this notice addresses —

- income tax withholding and reporting with respect to annual deferrals made to a § 457(b) plan;
- income tax withholding and reporting with respect to distributions from a § 457(b) plan;
- Federal Insurance Contributions Act (FICA) payment and reporting with respect to annual deferrals under a § 457(b) plan;
- employer identification numbers (EINs) used in connection with trusts established under § 457(g); and
- the application of annual reporting requirements to § 457(b) plan administrators and trustees holding assets of a § 457(b) plan in accordance with § 457(g).

This notice addresses only reporting and withholding rules that apply to § 457(b) plan participants who are or were employees of state and local governments or tax-exempt organizations and does not cover special reporting rules that may apply to § 457(b) plan participants who are or were independent contractors.

II. BACKGROUND

Section 457 provides rules for nonqualified deferred compensation plans established by eligible employers. State and local governments and tax-exempt organizations are eligible employers. They can establish either eligible plans that meet the requirements of § 457(b) or plans that do not meet the requirements of § 457(b) and that are therefore subject to tax treatment under § 457(f).

Section 1448 of the Small Business Job Protection Act of 1996, ("SBJPA"), 1996–3 C.B. 155, 212, amended § 457 by adding § 457(g), which requires that § 457(b) plans maintained by state or local government employers hold all plan assets and income in trust, or in custodial accounts or annuity contracts described in § 401(f), for the exclusive benefit of participants and their beneficiaries. Section 457(g) applies generally to assets and income held by a governmental § 457(b) plan on and after August 20, 1996. However, with respect to a governmental § 457(b) plan in existence on August 20, 1996, a trust (or a custodial account or annuity contract) was not required to have been established before January 1, 1999. Section 457(g) does not apply to a § 457(b) plan established by a tax-exempt organization that is not a state or local governmental entity.

Notice 98–8, 1998–1 C.B. 355, provides guidance regarding the amendments made to § 457(b) by the SBJPA. Following publication of the 1998 notice, the Service received additional inquiries regarding the statutory changes made in § 457(b) by the SBJPA and the Taxpayer Relief Act of 1997, Pub. L. No. 105–34. Specifically, taxpayers, employers, and plan administrators asked what employment and income tax reporting requirements apply with respect to § 457(b) plans and whether a trustee or administrator of a trust established under § 457(g) must file annual information returns relating to the trust, such as Form 990, Return of Organization Exempt From Income Tax, or an appropriate version of Form 5500, Annual Return/Report of Employee Benefit Plan.